

# **SUPREME COURT OF INDIA**

Messrs Matsushita Television and Audio (I) Limited

Vs

Commissioner of Customs

Appeal (Civil) 526 of 2002

(S. H. Kapadia and B. S. Reddy, JJ)

12.04.2007

## **JUDGMENT**

### **S. H. KAPADIA, J.**

This civil appeal under Section 35L(B) of the Central Excise Act, 1944, is directed against the Order passed by the Central Excise & Customs & Gold Control Tribunal (for short, 'CEGAT') dated 24.8.01. By the said Order the CEGAT (Tribunal) has dismissed the assessee's appeal.

A short question which arises for determination in this civil appeal is: whether the royalty payment was connected with the imported components of Colour TV and if so whether such royalty payment was includible in the assessable value of such components.

Appellants-assessee is a joint venture of M/s. Matsushita Electric Industrial Co. Ltd., Japan, (for short, 'MEI'). The predecessor of the appellants was M/s. Salora International Ltd. (for short, 'SIL'). In 1993, M/s. SIL had entered into an agreement with M/s. MEI for obtaining technical assistance and know-how. The technical assistance and know-how was assigned by M/s. SIL to the appellants. This was in 1996. In terms of clause 6.01, appellants were required to pay royalty at 3% on net ex-factory sale price of the colour receiver manufactured by them towards technical assistance rendered by MEI. In addition to royalty the appellants were also required to pay U.S.\$ 2 lakhs, as lump-sum

payment to MEI for transfer of technical know-how. Under the agreement, MEI agreed to assist the appellants by selling the equipment at commercial prices. Under the agreement appellants' predecessor imported components of colour receiver from M/s. B.M. Nagaro & Co. who in turn had procured components (bought-out items) from different manufacturers including those in Singapore.

By Adjudication Order NO.6/99 dated 20.5.99, the Adjudicating Authority loaded the value of the said components by 2% and 1.58% for the years 1996-97 and 1997-98 respectively. This was in terms of Rule 4(2) and Rule 9(1)(c) of the Customs Valuation (Determination of Price of Imported Goods) Rules, 1988 [for short, 'Valuation Rules, 1988']. The said Order confirmed by the Commissioner (Appeals) vide his Order No.683/2000 dated 15.11.2000. The said concurrent findings were also confirmed by the impugned judgment of the Tribunal. According to the impugned judgment, the assessable value of the components were required to be loaded with the cost of royalty payment as under the Agreement the appellants had agreed to pay to MEI a royalty at 3% on the net ex-factory sale price of the colour receiver manufactured by the appellants for the technical assistance rendered by MEI. According to the Tribunal, on bare reading of the Agreement it was clear that the royalty payment was related to components in view of clause 7.02. According to the Tribunal, the technical assistance under the Agreement was related to the components since under clause 7.02 it was stipulated that not only MEI would assist SIL in selling the components but MEI would also assist the appellants in approving the components which were bought-out items. Under the Agreement, samples of bought-out items were to be sent by the appellants to MEI for inspection and quality certification. Under the agreement, the bought- out items (components) could be used in the T.V. only if it was approved by MEI. Under the Agreement, MEI had to approve in writing the quality and the specifications of such bought-out items (components). In the circumstances, the Tribunal took the view that technical assistance extended not only to the supply of components but also to the approval of the components (bought-out items). Further, according to the Tribunal, the amount of royalty had to be included in the price paid for bought-out items (components). For the above reasons, the Tribunal held that royalty payment constituted consideration for technical assistance rendered by MEI and, therefore, the Department was right in including the cost of royalty payment in the assessable value of the components (bought-out items), duly imported. For the above reasons, the Tribunal dismissed the appellants' appeal. Hence this civil appeal.

This matter has been decided by all the authorities below and CEGAT only on interpretation of the various clauses containing in the Agreement dated 20.8.1993. Therefore, we quote hereinbelow the relevant provisions of the Agreement which are as follows:

## "TECHNICAL ASSISTANCE AND KNOW- HOW AGREEMENT"

### 1. DEFINITIONS

1.02 The term "Products" shall mean one or more of such models of the Item designed by MEI, as MEI regularly manufactures at its own and/or its subsidiaries/affiliates' factories and as shall be selected from time to time during the term hereof by mutual agreement of the parties hereto in writing, provided that MEI reserves the right to finally decide in selecting such specific models as

the products.

1.03 (a) The term "Net-factory Sales Prices" shall mean the sales prices billed by SIL of the Products to its customers in normal arm's length transaction exclusive of excise duties, custom duties, ocean freight and insurance, but including the cost of the standard brought out components (hereinafter defined) and the cost of the imported Components.

(b) In relation to the products sold other than in normal arm's length transaction, used, leased or otherwise disposed of by SIL, the prices equal to the arithmetic average of the Net Ex-factory Sales prices of the same products reported to MEI in the immediately preceding Calculation Period (hereinafter defined) shall be deemed to be the Net Ex-factory Sales Prices for such Products, but if there be no same Products so reported, then the Net Ex- factory Sales Prices for such Products shall be determined by mutual agreement of the Parties hereto.

1.04. The term "Technical Know-how" shall mean such technical information in written form as shall be specified in Section 3.01 hereof, embodying technical know-how and data required for the manufacture of the Products.

1.05. The term "components" shall mean component, parts, material and/or sub- assemblies comprising the Products.

## 2. RENDERING OF TECHNICAL ASSISTANCE

2.01. MEI agrees to render to SIL the technical assistance regarding the manufacturing of the Products in the manner provided in Clause 2 hereof. To the extent that both parties deem necessary, the technical assistance to be rendered by MEI as aforesaid shall comprise the training to effectuate the following items (hereinafter called "Technical Assistance"):

1. Advice and instruction for the manufacture of the Products;
2. Advice and instruction on installation, operation and maintenance of Production Equipment used for the manufacture of the Products;
3. Advice and instruction on factory layout used for the manufacture of the Products; and
4. Other necessary advice and instruction.

2.02. The Technical Assistance for the manufacture of the Products shall be actually rendered in the manner hereinbelow specified.

(A) During the term of this Agreement upon request of SIL and by consent of MEI thereto, MEI will permit employees of SIL to visit the manufacturing department concerned of MEI and/or MEI's subsidiaries/affiliates which manufacture the Products, for a period MEI deems necessary, for training in the process of manufacturing the Products.

(B) During the term of this Agreement, upon request of SIL and by consent of MEI thereto, MEI will send the engineers of MEI and/or MEI's subsidiaries/affiliates to SIL's factory manufacturing the Products hereunder for a period MEI deems necessary to give instructions to the employees of SIL engaged in the manufacture of the Products.

(C) All costs and expenses incurred for the Technical Assistance as referred to in (A) and (B) of this Section 2.02 hereof (including those for accommodation, transportation, and both way air coaches and salaries and allowances payable for MEI (including MEI's subsidiaries/affiliates)'s engineers and SIL's Employees) shall be paid by SIL in United States Dollars. In case any costs and expenses payable by SIL to MEI for the Technical Assistance herein contained be prepaid by MEI, SIL shall reimburse to MEI in United States Dollars promptly after receipt by SIL of MEI's invoice therefore. Details of the terms and conditions for the Technical Assistance of MEI (including MEI's subsidiaries/affiliates)'s engineers visiting SIL's factory and SIL employees visiting MEI (including MEI's subsidiaries/affiliates)'s factory, as the case may be, shall be confirmed in writing between the parties hereto prior to such visit.

#### 4. USE OF TECHNICAL ASSISTANCE AND TECHNICAL KNOW HOW

4.01. During the term of this Agreement MEI agrees to grant to SIL a non-exclusive and non-transferable licence to use the Technical Assistance and the Technical Know-how manufacture of the Products at SIL's factory in India and for sale of such Products throughout India. In the event this Agreement expired, however, MEI agrees to grant to SIL a non- exclusive and non-transferable licence to use the Technical Assistance and the Technical Know-how for manufacture of the Products at SIL's factory in India only for the orders booked from SIL's customer in India during the terms of this Agreement.

4.02. The Technical Assistance and the Technical Know-how made available to SIL hereunder shall be used only for SIL's own manufacture of the Products at its own factory in India, and SIL undertakes that such Technical Assistance and Technical Know-how made available to SIL hereunder shall be neither directly or indirectly transferred nor be made available to any third party. The term "third party" used herein shall mean any party who shall not sign this Agreement.

#### 6. REMUNERATION

6.01. Payment of the Technical Assistance:

A. In consideration of the Technical Assistance rendered by MEI under Clause 2 hereof and the license granted under Clause 4 hereof, SIL shall pay to MEI the royalty at the rate of three percent (3%) on the Net Ex-factory Sales Prices of the Products manufactured and sold, used, leased or otherwise disposed of by SIL

Herein.

B. SIL agrees to forward to MEI written royalty reports in a form attached hereto as EXHIBITS A and B, which shall be audited and certified by a certified public accountant retained by SIL, within ninety (90) days after the end of each Calculation Period, setting forth the number of all Products manufactured and sold, used, leased or otherwise disposed of by SIL during the immediately preceding Calculation Period, and also showing computation of the royalty payable pursuant to the provisions of this Clause 6 and deduction of the withholding tax as referred to in Section 6.01-E below.C to G.....

## 7. PRODUCTION EQUIPMENT AND COMPONENTS.

### 7.02. Components:

A. In addition to the technical assistance herein contained, MEI will assist SIL as much as practicably possible in manufacturing the Products by selling, at the reasonable request of SIL, the Components to SIL.

B. SIL may, if it so desires, use in manufacturing the Products certain Components available from sources other than MEI, if SIL first sends reasonable quantities of samples of such components to MEI for inspection and if then MEI approves in writing the quality and the specifications of such Components.

7.03. Sale and purchase of the Production Equipment and the Components supplied by MEI pursuant hereto shall be made at commercial prices under payment and other terms to be agreed upon between MEI and SIL and subject to the necessary approval and the concerned authorities of the Japanese Government or Indian Government, as the case may be. Specifically payment of the purchase price of the Production Equipment and the components so supplied by MEI to SIL shall be made through the Japanese shippers designated by MEI under the terms and conditions to be agreed upon among the parties concerned.

7.04. Supply of the Production Equipment and Components from MEI to SIL hereinabove set forth is for the sole purpose of SIL's own manufacturing of the Products hereunder for itself, and unless otherwise agreed in writing by MEI, any item of the Production Equipment and the Components supplied by MEI hereunder, unless otherwise agreed by MEI."

On reading the above agreement, the following features emerge. Under Clause 1.03 the term "Net-

factory sale price" has been defined to mean the sale price billed by the appellants for its products to its customers in normal arm's length transaction exclusive of taxes, freight and insurance, but including the cost of the bought-out components and the cost of the imported components. Under Clause 1.04 the term "Technical Know-how" was defined to mean technical information required for the manufacture of colour T.V. as specified in Clause 3.01. The technical know-how which was agreed to be furnished to the appellants was to consist of quality control standard and specification of the components to be used in the manufacture of T.V. sets. Further, under Clause 2.01 it was agreed that MEI shall render to the appellants the technical assistance regarding the manufacture of the T.V. sets in the manner provided in the said clause. Under the said Clause 2.02(C), all costs, charges and expenses, incurred by the appellants for technical assistance, was to be paid by the appellants in U.S. Dollars. Further, under Clause 4.01, MEI agreed to grant to the appellants a licence to use the technical assistance and the technical know-how for the manufacture of the colour T.V. at the appellants' factory in India and also for sale of such products throughout India. Under Clause 6.01, in consideration of the technical assistance to be rendered by MEI and in consideration of the licence to be granted by MEI to the appellants it was agreed that the appellants shall pay to MEI the royalty at the rate of 3% on the net ex-factory sale price of the colour T.V. manufactured and sold. Further, it was agreed that in addition to the technical assistance, MEI would assist the appellants in the manufacturing of the colour T.V. by selling the components to the appellants. Under the Agreement, the parties further agreed that if the appellant desired to make use of bought-out components it can do so provided the said components are forwarded to MEI for inspection and if MEI approves the quality and the specifications of such bought-out components then alone the appellant would be free to use such components in the manufacture of colour T.V.

The question which arises for consideration in this civil appeal is: whether royalty payment was connected with the imported components. Under Rule 9(1)(c) of the Valuation Rules, 1988, only such royalty which is relatable to the imported goods and which is a condition of sale of such goods alone could be added to the declared price. However, in the present case, payment of continuing royalty was payable at the rate of 3% of the net ex-factory sale price of the colour T.V. exclusive of taxes, freight and insurance but including the cost of imported components. In other words, the royalty payment was to be computed not only on the domestic element of the net sale price of the colour T.V. but also on the cost of imported components. A bare reading of the agreement shows that payment under the said agreement related not only to the production of the goods in India but also to imports. In some of the decisions cited on behalf of the assessee, we find that the net ex-factory sale price of the finished products expressly excluded the cost of imported components. On the other hand, in the present case, the cost of imported components was expressly included in the net ex-factory sale price of the colour T.V. Further, when payment to MEI was at the rate of 3% of the sales turn over of the final product, including cost of imported component, it became a condition of sale of the finished goods. Hence, in this case both the conditions of Rule 9(1)(c) of the Valuation Rules, 1988, are satisfied.

For the above reasons, we find no merit in this civil appeal and the same accordingly stands dismissed with no order as to costs.